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SUBJECT: PRESIDENT'S STATE OF THE UNION SPEECH: ECONOMIC  
SUCCESES, MILITARY BUILDUP, AND CRITICISM OF MONOPOLISTS  
AND ELITES

Classified By: AMBASSADOR ANNE E. DERSE PER REASONS 1.4 (B,D)

11. (C) SUMMARY: In an October 23 cabinet meeting, President Aliyev detailed the social and economic successes of the first nine months of 2007. In a prepared statement, Aliyev commended the Government of Azerbaijan's (GOAJ) efforts to create jobs, develop the rural areas and improve the living standards and incomes of citizens. He commented on the growing international presence of the State Oil Company and the negative effects of Barmek, a Turkish electricity distribution company accused of fraud. Aliyev stated proudly that Azerbaijan is seriously engaged in military expansion and in 2008 the military budget will increase to USD 1.3 billion. Aliyev warned unnamed monopolists that he was monitoring closely price increases and scolded the Interior Minister for being soft on "hooligans," not obeying traffic rules and for tinting their automobile windows. Aliyev's populist speech appears timed to appeal to the general public in the early run-up to the 2008 presidential elections. END SUMMARY.

#### ECONOMIC SUCCESES

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12. (SBU) On October 23 President Aliyev held a cabinet meeting at which he reviewed the socio-economic results of the first nine months of 2007. The ministers of Energy and Industry, Taxation, Transportation and Environment and Ecology also spoke at the meeting. President Aliyev read a prepared statement to begin the meeting, followed by the three ministers' presentations and then President Aliyev closed the meeting with additional prepared statements.

13. (SBU) In his upbeat assessment of the country's development, President Aliyev stated that both economic and industrial production growth have increased 27 percent. Aliyev highlighted his concerns with increasing inflationary pressures, citing the current CPI rate of 16 percent and stated that "it very much disturbs us, and we shall try to lower the rate of inflation as much as possible." Aliyev continued that "there are subjective reasons which are necessary to eliminate, in particular, monopolism, unhealthy competition and, as a result of this, increases in prices."

14. (SBU) In a possible warning to unknown economic operators, the President stated that monopolists "have to be punished very seriously." He said that "I regret to see monopolistic trends ruling in some sectors of import and local production activities. We have to fight against these trends, which will help curbing inflation and keeping it at a single-digit level." President Aliyev also reiterated later in his speech his concern about inflationary pressures, stating that "I am concerned about the recent increase of inflation at 15-16

percent. I reiterate it again, there are some natural and artificial reasons for that. We have to take administrative measures and apply sanctions against companies causing these problems." The President also dispelled rumors about possible utility price increases in 2008.

#### RISING INCOMES

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15. (SBU) The President highlighted that GDP per capita at the end of 2007 should reach USD 3,500 and "as a result of additional economic reforms in 2008," should total USD 4,500 by 2009. Aliyev attributed this increase in per capita income to Azerbaijan's national oil strategy, economic reforms, creation of new industrial fields, and strengthening of economic potential.

16. (SBU) The President stated that incomes of Azerbaijanis have increased by 40 percent, with real incomes increasing by 22 percent. He characterized income growth as the "rise of welfare of the Azerbaijani people" and said that the increase is proof that GOAJ economic reforms are yielding results. Aliyev stated that Azerbaijan's currency reserves currently total USD 6.3 billion, further enabling the GOAJ "to carry out the economic reforms more efficiently." Stating that in the coming years the country's resources will grow, President Aliyev attributed the positive results to the "successful performance of Heydar Aliyev's oil strategy," which will be an important factor to strengthen the economy.

17. (SBU) Turning to the 2008 state budget, Aliyev recognized that the budget has increased significantly over the past several years. Aliyev said that the budget expenses of 2008 will total USD 10 billion, calling this amount a "a great

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achievement, a great figure." He compared the current budget total to the 2003 state budget amount of USD 1.5 billion. Aliyev again attributed this increase in budgets to a "successful oil strategy, and a result of deepening economic reforms and financial discipline," concluding that as a "whole, it is a sign of economic development." Aliyev noted that Azerbaijan had the opportunity to utilize foreign financing, adding that even if Azerbaijan does not choose this step Azerbaijan "will not suffer from this."

#### INFRASTRUCTURE SPENDING AND REGULATION

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18. (SBU) Aliyev stated that the amount of investments in the 2008 state budget exceeded USD 3 billion, noting that Azerbaijan "can successfully realize any industrial, economic, infrastructure project." Aliyev recognized that Azerbaijan required extensive modernization and that the country's entire infrastructure system should be updated and brought to an advanced level. He concluded that the 2008 budget is "the budget both of social and investment orientation." Later in his speech, Aliyev stated that the Azerbaijan Investment Company (AIC) needed to work "more effectively" in order to realize concrete non-energy sector projects between AIC and foreign partners.

19. (SBU) Later in the meeting, Aliyev commented on the booming construction sector and the impact of a building collapse in September. He stated that state control over the construction sector shall be "even stronger." He recognized that "there are a lot of problems in this area" that the GOAJ was "unhappy about many issues" and that the "tragedy triggered a serious investigation in the sector" leading to the discovery of many irregularities. He acknowledged that unlicensed buildings are being constructed and that more attention need to be paid to this issue in order to stop abuses and illegal actions. Aliyev concluded that "all violators will be punished seriously."

¶10. (SBU) Turning to social issues, Aliyev said that the GOAJ has taken important steps to resolve social questions, stating that monthly average wages in Azerbaijan had reached USD 230 and that the average pension totaled almost USD 70. Aliyev said that 294,000 citizens receive social allowances and that each family receives social assistance of approximately USD 100 per month. He said that the number of people living in poverty was likely to decline in 2008 and that the government planned to raise the minimum salary and pensions next year.

#### ECONOMIC DEVELOPMENT OF REGIONS AND NON-ENERGY SECTOR

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¶11. (SBU) Aliyev stated that the government's program for development of the regions "is being successfully carried out," noting that "the class of businessmen is becoming stronger, new factories and plants are opening, infrastructure projects are being carried out, and power stations are being built." He said that as a result of the GOAJ's economic reforms and the successful regional program, 610,000 jobs have been created in the past four years, including 430,000 permanent jobs. Aliyev stated that his promise of 2003 to create more employment "has become a reality" and that the problem of unemployment will be "solved." Aliyev stated that all the new jobs had been created in the non-energy sector.

¶12. (SBU) Later in the cabinet meeting, President Aliyev stated that in 2004 it was impossible to calculate all the issues that need to be solved in the government's regional development program. He said that he instructed the government to plan ahead, allocate financial resources and include all the work to be done into the regional development program. He highlighted the need for executive bodies and responsible agencies to be clearly identified, which will "ensure development of the non-oil sector."

¶13. (SBU) Aliyev also trumpeted the government's success in reforming the education system, including the construction of 1,200 schools and the reforms carried out in higher educational institutions, construction of public health structures, improvement of health care, creation and restoration of now scientific research centers. In addition, he said that the government had built 13 sports complexes and restored many cultural and historical sites. He said that the GOAJ was implementing "ecological programs," especially

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on the Absheron Peninsula, that will alleviate the polluted areas and create improved conditions. Calling the protection of environment a priority, Aliyev said that the government had already allocated funding in the budget and President's Fund to implement the clean-up effort.

#### BUILDING OF DEFENSE INDUSTRY

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¶14. (SBU) Aliyev stated proudly that Azerbaijan is "seriously engaged in military expansion and that each year the military budget increases." In the current year, according to Aliyev, the military budget has increased to USD 1 billion and next year will increase to USD 1.2-1.3 billion. Aliyev stated that Azerbaijan "lives in a condition of war, our lands are under occupation, insincere behavior of the aggressor, the tightening of the process of negotiations and the creation of artificial obstacles, certainly, compel us to give more attention to military issues."

¶15. (SBU) Aliyev stated that Azerbaijan "shall do it (increase military spending), and nobody can reverse us from this path," adding that "it is our sovereign right, and Azerbaijan should be ready to release the lands from occupational forces by any means -- for this purpose, the powerful economy and strong army are necessary." Aliyev also noted the creation of a domestic military industrial complex,

stated that in the near future Azerbaijan shall see the production of its first military hardware.

## ENERGY

¶16. (SBU) In the energy area, Aliyev stated that Azerbaijan continues to participate in numerous energy projects and has become a huge gas exporting country. He added that "the factor of gas for energy security in the world currently has a more important position than the oil factor." He said that according to latest estimations, the reserves of natural gas in Azerbaijan total approximately 2 trillion cubic meters, which he said "is enough for us at least about 150 years." Aliyev quickly added that Azerbaijan will "provide gas export to other countries," noting that Azeri gas goes to markets in Georgia and Turkey, and in "future will be delivered to the markets of other countries." Aliyev stated that Azerbaijan's gas strategy "opens for us extra economic opportunities, will notably strengthen regional cooperation, and will raise the political weight of Azerbaijan."

¶17. (SBU) Later in his speech, President Aliyev recognized that Azerbaijan has been very successful in the oil sector, noting that it has "accomplished all the tasks" planned. He said that the GOAJ had ensured the country's energy security, and was going to participate in solving energy security issues of the neighboring states and the Europe. He said that the government's "thoughtful policy, transparency of the oil sector, and just distribution of revenues" were responsible for poverty reduction.

¶18. (SBU) Later in the meeting, the President recognized the State Oil Company's (SOCAR) improving credit rating, enabling SOCAR to attract international financing for domestic and international projects. Aliyev said that SOCAR's role "will definitely expand our economic opportunities and Azerbaijan will act as a foreign investor in other countries," reiterating that the GOAJ would do its best to attract foreign investors to Azerbaijan. The President highlighted SOCAR's investments in Georgia, Turkey and Eastern Europe.

¶19. (SBU) President Aliyev also made comments on the Barmek electricity distributor case later in his remarks. He noted that Barmek was in Azerbaijan "to steal from the Azerbaijani population" and that it made no capital investments. He believed that since the GOAJ assumed control, Azerbaijan had received "great results." According to Aliyev, the GOAJ is building new power stations to ensure regular electricity supplies for its citizens.

¶20. (SBU) Aliyev stressed that Azerbaijan's successful foreign policy and acceptance of its national economic, political, energy and transport initiatives will strengthen the country and transform it into a regional center. He reiterated that any "project cannot be realized in region without participation of Azerbaijan." Aliyev stated that the Baku-Tbilisi-Kars railway construction will start soon, calling it "our largest, historical achievement."

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## ANTI-CORRUPTION EFFORTS?

¶21. (SBU) At the end of the cabinet meeting, President Aliyev made uncharacteristic comments on the conduct of government officials and the general public. Aliyev stated that the "law should be equal for everyone. No one should have special status. No one in my family does." Aliyev continued that he does not like "the events of an unexplained nature, that are not in line with our national character and traditions." He urged all public officials to be "sensitive to ethics and norms" and not to engage in activities that can damage the morale and image of the government, adding that

public officials and people on TV should be modest and live in accordance with the national spirit.

¶22. (SBU) Aliyev also questioned how certain citizens were considered "untouchable" for traffic crimes while others are being punished for even minor violations. Remarking "I don't accept this," Aliyev said that he would instruct the Ministry of Internal Affairs to take care of the disparity, calling the law breakers "hooligans."

¶23. (SBU) Turning to more ordinary issues, Aliyev said he has repeatedly ordered the removal of automobile window tinting. He said that the owners of these cars are "officials, MPs, their relatives or big businesses." Aliyev continued that "why do they hide behind the tinting? Are they afraid of someone?" He said that before he became president he did not travel in vehicles with tinted windows and "would stop for every red light." Aliyev stated that "these people are not paying fines, ignore rules. I will punish the people they rely on." The following day, local Baku police could be seen throughout the city stopping all cars with tinted windows and removing window tinting.

¶24. (C) COMMENT: As in previous cabinet speeches, much of President Aliyev's speech touched on the economic successes of the past nine months without providing extensive details, especially regarding the number of jobs created - a major 2003 presidential campaign promise. Aliyev's positive spin on the state of economic growth comes as Azerbaijan is just beginning to reap the economic and financial benefits of its growing energy resources. His ominous words against unnamed monopolists are uncharacteristic and interesting given his and many of his officials' close connections to many of the large domestic companies operating in Azerbaijan. The President appeared to hint at undefined economic measures, possibly price controls, to moderate increases in consumer prices. President Aliyev may be taking a more populist approach by attacking higher prices, monopolies, and "hooligan" officials to appeal the general public in the early run-up to the 2008 presidential elections.  
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